UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
REGION 10
1200 Sixth Avenue
Seattle, WA 98101

July 19, 2010

Reply To
Attn of: OEA-095

SUBJECT: Linnton Plywood Association – Preliminary Ability to Pay Analysis

FROM: Lloyd B. Oatis
(SEE) Financial Analyst

Lloyd B Oatis

TO: Lori Cora
Assistant Regional Counsel

Background

Linnton Plywood Association (PRP) is a cooperative corporation (Co-Op) whose owners included the former workforce of the business. The PRP owned and operated a plywood manufacturing and processing facility at 10504 NW St. Helens Road, Portland, Oregon. The facility is adjacent to the Willamette River at approximately river mile 4.5. Information in EPA's position indicates that releases of hazardous substances have occurred at the facility and have migrated to the Willamette River and, thus, the PRP is potentially responsible for response costs at the Portland Harbor Superfund Site in Portland, OR. The Association has not operated as a manufacturing facility since 2001. The PRP currently rents the property for equipment storage and a sand and gravel operation. The purpose of this analysis is to estimate the amount that the PRP can contribute to the clean-up of the Portland Harbor Superfund site. The amount of cleanup liability for the PRP (before consideration of ability to pay) has not been determined.

An ability to pay analysis for a business looks at the business' (1) ability to generate profits and cash flow, (2) ability to raise funds from debt (and correspondingly the ability to repay the debt), (3) insurance proceeds that covers the clean-up, and finally (4) the sale of assets that are no longer used or needed in the on-going operation of the entity. Each of these sources will be addressed as to the contribution that may be made to the clean-up. Based on the following analysis, Linnton Plywood Association appears to have approximately $3,900,000 in potential funds to contribute to the cleanup. The potential funds come from potential insurance proceeds and potential net proceeds from the ultimate sale of the real property owned.

Documentation Used in the Analysis

Documentation used in this analysis include:

Correspondence from William Hutchinson to Lori Houck Cora with the following dates:

- 10/02/2009
- 10/30/2009
- 3/24/2010
- 4/19/2010
- 5/29/2010
- 6/04/2010

The above included attachments that provided the PRP's Federal Tax Returns for 2007 and 2008, unaudited financial statements for periods ending 9/30/09, 3/31/09, and 3/31/08, insurance policies and related correspondence, Articles of Association and Association By-laws, and a worksheet detailing the current Retains and stock holdings of Linnton Plywood Association

Internal EPA e-mail from Lori Cora to Kristine Koch and Lloyd Oatis dated 7/12/2010

Multnomah County, Oregon Property Information and Tax Summaries for three parcels of real property owned by Linnton Plywood Association in the Portland Harbor area

Current Operations

The plywood manufacturing business on the site ceased about nine years ago in 2001. Currently, the operations revenue consists principally of rental income of $350K to $400K annually. The corresponding operating expenses were almost equal to that revenue in year ending 3/31/2009 (the latest complete year we have information). The same is true for the previous year except there was an item for professional services for $176K which appears to be the primary reason for the loss for the year ending 3/31/2008. For both of the above years, the PRP did not pay property taxes on owned parcels. The property tax liability shown on the financial statements, dated 9/30/2009, and provided in the correspondence from Mr. Hutchinson dated 3/24/2010 and was $200,046. The details behind the financial statements is not known; however, the most current information from the Multnomah County tax records as of 7/15/2010 show the property tax liability plus interest on the subject parcels is $337,405.

Based on the information available and summarized in the preceding paragraph, it appears that there are no funds available from the on-going operational cash flow of the PRP. The current operations appear to be in a "caretaker" state such that the PRP is maintaining the rental business until the property can be sold and the CO-OP assets distributed and dissolved.

Insurance Proceeds

Based on correspondence from William P. Hutchinson (attorney for PRP) dated 10/2/09, 10/30/09 and 3/24/10, the PRP may have insurance coverage of $100K per year from1966 to 1985 for a total of $1,900,000. Further, the policies have been confirmed that they are not "wasting policies" which indicates that remedial investigation and remedial costs (noted previously as $400,000 can not be deducted from insurers liability. The insurer (Liberty Mutual) contends that $62,959 can be deducted from the proceeds leaving a total of $1,837,000 as the amount that may be recovered.

Based on information (letter dated 6/4/2010 from William Hutchinson and subsequent conversations between Mike Farnell and Lori Cora), Liberty Mutual has offered to settle the claims for $500,000 based the years 1966-1971. Liberty Mutual, the successor insurance company, has taken the position that policies after 1971 contain a pollution exclusion and there is no coverage for the last fourteen years or $1.4 million. Mike Farnell believes that the $500,000 mentioned above is the likely minimum insurance proceeds that could be recovered under the policies. In addition, he has asserted that it is highly likely that some or all of the coverage under policies purchased between1971–1982 can also be recovered for an additional $1,000,000. **The remaining $400,000 +/- has more risk. Based on the current assessment, the insurance proceeds may be between $1.5 million and $1.9 Million.**

In his 6/4/2010 correspondence, Mr. Hutchinson said that the Oregon Department of State Lands has filed claims against their insurance under the aquatic-lands lease held by the PRP. The amount of the claim or years covered is not known. However, this claim may overlap the subject claim of this analysis.

Sale of Assets and Distribution of Proceeds

Asset Valuation - The principal asset and source of funds for Linnton Plywood Association is the site at Portland Harbor. The current market value of the land and buildings at the site is not known since there is not a current offer on the property. However, in 2009 BP West Coast Products, LLC (BP) had made an offer for $6.5 million. Since that time, BP has withdrawn its offer principally due to the inability to resolve the CERCLA claims and claims of other agencies. BP may or may not be a viable purchaser in the future; however, the offer does set an approximate value for the property that will be considered as a basis for this analysis. The Taxable Real Market Value for property tax purposes is $6,524,250 according to the Multnomah County, Oregon tax assessment records. **Therefore, we will maintain the value at $6.5M for purposes of this analysis.**

Third Party Creditors – According to Mr. Hutchinson's letter dated 10/20/2009, the PRP will owe approximately $600K to third party creditors. In Mr. Hutchinson's 3/24/2010 letter he stated that the $600K included attorney's fees, expected operating losses and unpaid property taxes. Further, he stated that "the Association continues to incur losses of approximately $15,000 per month and accumulates unpaid property taxes and interest totaling approximately $325,000."

From the financial statements for FY ending 3/31/09 and six months ending 9/30/09, it appears that the PRP is actually profitable rather than accumulating the loss of $15K per month that Mr. Hutchinson indicated. Also, it appears that the PRP has not paid all the property taxes owing since 2006. **The total property taxes and interest at 7/15/2010 is $337,405 according to the Multnomah County, Oregon records. Since the attorney's fees are unknown, the estimated amount due to third parties is $400K.** If the attorney's fees or other items not mentioned are higher than $63K, this total will likewise increase

If we assume that the Association will liquidate when the property is sold, based on the latest Balance Sheet available dated 9/30/2009 there was a cash surplus of approximately $160K (includes Cash Rents Receivable, Accounts Payable and Insurance Payable) not considering Property Taxes. **This amount will not be considered due to the unknown amount of costs to liquidate the business.** However, there may be funds available from this source.

<u>Closing Costs</u> - **The explanation in Mr. Hutchinson's 3/24/2010 letter for closing costs to be incurred upon the property sale estimated at $600K appears reasonable and will be a reduction of the amount available from the sale.** These costs include broker's fees, escrow, title insurance, and legal fees required to be paid by the seller.

<u>Share Redemption</u> - According to Schedule F of the correspondence from Mr. Hutchinson dated 3/24/2010, 126 Members are holders of outstanding shares. Therefore, the share redemption is valued at $630K (126 X $5K = $630K). The amount shown on financial statements for Common Stock is $408K. The difference is that this represents the original paid in stock less Treasury Stock. The amount paid to Members redeeming earlier was apparently greater in value than the par value. **Therefore, the amount to be redeemed is $630K.**

The shares provided the original investment and operating funds for the PRP. It is argued by the PRP that this share redemption should be returned to the members exclusive of any returns as a stipulation of the settlement offer made in 2009. These shares are unlike shares in a corporation in that shares had to be owned in order to work at the mill. In addition, there were no dividends or other profit sharing during the Association's operations. Finally, since there was no reason to buy additional shares since only one person could qualify to work with a share, the shares could be looked at as a cost of employment without possibility for direct financial returns (except employment), the shares should be considered as an amount that should have a preference for return to the members. While this argument (to return the par value to Members) is not as overwhelmingly persuasive as the one for Retains below, I believe that it is an equitable treatment of the remaining Members.

Retains – According to Mr. Hutchinson's letter dated 10/2/2009, there are 199 current and former Members (some are no longer stockholders) that have outstanding retains. Since the Association could not issue new stock (as mentioned in the above section), the operating capital was provided by withholding some of the Members' profits but including them as individual earnings as if they had been received. Records were maintained by member and the result is an outstanding balance of **$2,484,000 is owed to the Members** according to Mr. Hutchinson's letter and schedules dated 3/24/2010. This amount does not include any interest on the original amounts recorded over the years of operation. **Since the members have been taxed on the amounts apportioned to them, the Retains are a legitimate priority amount to be paid out of future sales proceeds.**

Remaining Sales Proceeds – The remaining proceeds, if any, will consist of funds remaining from property sales receipts after payments of all liabilities, closing costs, share redemption and Retains. These proceeds will include the net amount of all the preceding items under the heading "**Sale of Assets and Distribution of Proceeds".** In his letter dated 10/2/2009, Mr. Hutchinson estimated that this amount at $1.8M. He indicated that this remaining amount will be distributed "… to members with Retains on the books of LPA under a formula that recognizes the appreciation in the property during the time these members were working but not getting paid their Retains."

If it is felt that Mr. Hutchinson's rationale is legitimate and that all or a portion of the remaining sales proceeds should be given to the Members, this item can be totally or partially disregarded. This would leave primarily the insurance proceeds as the contribution from Linnton Plywood Association. However, for purposes of this analysis the remaining sales proceeds will remain as a recoverable item that may be used for cleanup. It appears that the nature of the remaining sales proceeds is the net profit of the sale after all obligations have been satisfied. The principal consideration for treating these funds as belonging to the Members is that they waited for many years for the Retains (which had been taxed) and original stock purchase with no receipt of time value of money.

An estimate of the Remaining Sales Proceeds based on the latest purchase offer (that has been withdrawn) of $6.5M results in an estimated total for Remaining Sales Proceeds of $2.4M as follows:

$Mln.		
Sales Price		***6.5***
Less: Third Party Creditors	*(.4)*	
Less: Closing Costs	*(.6)*	
Less: Stock Redemption	*(.6)*	
Less: Retains	*(2.5)*	
Total Deductions from Sales Price		***(4.1)***
Remaining Sales Proceeds		***2.4***

Conclusions

The sources of funds from Linnton Plywood Association to participate in the cleanup of the Portland Harbor are primarily from insurance and the sale of real property assets. The estimated recovery amount is $3,900,000 (insurance - $1.5M; property sale - $2.4M) based on the following:

As discussed above, the insurance proceeds are probably in the range of $500,000 and $1,900,000. According to an insurance coverage expert, recovery for 15 years of coverage appears likely, thus, could be about $1,500,000.

After sale of the property and pay off of creditors, sales closing costs, and Member obligations approximately $2.4M may be available for contribution to the cleanup costs. This is based on a sales price of $6.5M and estimated pay off costs of the above items.

Risks

Some risks and considerations for recovering the $3.9M estimated above include:

- Finding a willing buyer for property to pay in the range of $6.5M in a softer market than the previous offer
- Significant delay in finding buyer for property
- Not able to negotiate a settlement with insurance company for above estimated amount. Litigation cost and risk in pursuing insurance settlement
- Oregon Department of State Lands may have some claim against the insurance proceeds under aquatic land lease with PRP resulting in sharing some proceeds with them.
- Inability to reach settlement with PRP regarding the "Remaining Sales Proceeds". This may lead to sharing these proceeds with Members thus reducing recovery amount
- There may be more costs under third party creditors as estimated in Mr. Hutchinson's letter of 3/24/2010